IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1378

JAPAN LINE, LTD.; KAWASAKI KISEN KAISHA, LTD.; MITSUI O.S.K. LINES, LTD.; NIPPON YUSEN KAISHA; SHOWA LINE, LTD.; and YAMASHITA-SHINNIHON STEAMSHIP CO., LTD.,

Appellants,

—v.—

COUNTY OF LOS ANGELES; CITY OF LOS ANGELES; and CITY OF LONG BEACH,

Appellees.

ON APPEAL FROM THE SUPREME COURT OF THE STATE OF CALIFORNIA

BRIEF OF INSTITUTE OF INTERNATIONAL CONTAINER LESSORS, LTD., AS AMICUS CURIAE

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August 25, 1978

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BRIEF OF INSTITUTE OF INTERNATIONAL CONTAINER LESSORS, LTD., AS AMICUS CURIAE

The Institute of International Container Lessors, Ltd. ("IICL") submits this brief *amicus curiae* with the consent of the parties.[1] IICL, a Delaware corporation authorized to conduct activities and with principal offices in the City and State of New York, is the trade association for the international marine cargo container leasing industry.

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[1] Copies of Appellants' and Appellees' letters of consent are submitted with the signature copy of this brief.

Interest of IICL

IICL's members lease marine cargo containers (hereafter generally "containers") to ship lines for use in the worldwide transportation of goods. Containers are now the principal means for marine transportation of manufactured products and also play an increasingly significant role in ocean transport of certain raw materials and agricultural products. The estimated world population of containers is approximately 2.1 million (measured in twenty foot equivalents or "TEU"). Nearly one-half of these are owned by leasing companies, and the remainder are owned by the ship lines themselves.[2]

IICL's membership consists of both foreign and United States leasing companies. Five of IICL's nine members are United States corporations; the other four are foreign corporations.[3] This appeal concerns imposition of a California local personal property tax on the containers of foreign owners. IICL's foreign members are concerned by the application of the tax to them, but IICL's United States members are even more concerned because of the threatened retaliation by foreign countries, if the tax is upheld. Such retaliation is expected to take the form of property taxes imposed exclusively on the containers of United States owners. IICL's members therefore have a direct and substantial interest in the subject matter of this appeal and in reversal of the court below.

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[2] Approximately 700,000 TEU are owned by members of IICL; of these, approximately 455,000 are owned by United States members. Approximately 150,000 TEU are owned by other United States leasing companies, not members of IICL. United States leasing ownership is thus about 600,000 TEU. Total United States ownership, including both leasing companies and ship lines, is about 1,000,000 TEU. See page 5 and note 9 below. See also 12 *Containerisation International* 15 (No. 5, May 1978).

[3] A list of members is attached as Exhibit A.

ARGUMENT

I.

The Nature of the Container Industry, Shipping and Leasing, and the Magnitude of United States Interests at Stake.

Container shipping was begun in the late 1950's by Sea Land Service, Inc., a United States ship line which also appears in this appeal as *amicus curiae*. Container shipping did not begin in volume, however, until the middle or late 1960's. The world population of containers increased from approximately 250,000 TEU in 1968 to 2.1 million TEU in 1978, an increase of over 700%.

Containers are intermodal, that is to say, they can travel equally well by ship, on a chassis behind a tractor over the road, or on a railroad flat car. They are, nevertheless, unquestionably marine instruments. This is evidenced by the fact that container regulation and technology are dominated by marine bodies and concepts.[4] At least one leg of

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[4] The United Nations body principally concerned with containers is the Inter-governmental Maritime Consultative Organization ("IMCO") through its Sub-committee on Containers and Cargoes. United States government bodies principally concerned with containers include the State Department Working Group on Containers and Multimodal Transport of the Subcommittee on Safety of Life at Sea of the Shipping Coordinating Committee, the Coast Guard, the Maritime Administration, the Customs Service, and the Federal Maritime Commission. The Coast Guard administers the International Convention on Safe Containers (CSC) on behalf of the United States. See *International Safe Containers Act: Hearings on H.R. 8159 Before the Subcommittee on Coast Guard and Navigation of the Committee on Merchant Marine & Fisheries*, 95th Cong., 1st Sess. 215-247 (1977). The recognized classification society for containers in the United States is the American Bureau of Shipping; the same role is performed in other countries by their maritime classification societies, e.g. Lloyds Register Industrial Services in the U.K.,

virtually every trip made by a container involves a sea voyage. Accordingly, it has become generally accepted that containers are part of the ship, either structurally or as part of the ship's gear. See *Pittston Stevedoring Corp.* v. *Dellaventura*, 544 F.2d 35, 53 (2d Cir. 1976); *Leather's Best, Inc.* v. *SS Mormaclynx*, 451 F.2d 800, 815 (2d Cir. 1971); see also Rev. Rul. 60-185, 1960-1 C.B. 412; N.Y. Sales Tax Reg. §528.9 *Commercial Vessels*.

The modern containership is designed solely for the transport of goods by container, and container owners, both ship lines and leasing companies, jealously guard their containers' status as Instruments of International Traffic in order to avoid customs duty.[5] They can do this in the United States only by ensuring that all trips are part of a direct import or export move or are made to reposition for an export move.[6] Containers are not generally used for domestic commerce simply because it is less expensive to ship goods by ordinary tractor/trailer truck than by container, if a trip does not involve a sea voyage.[7]

Bureau Veritas in France. Other organizations performing similar functions in the United States include International Cargo Gear Bureau, Inc. and Marine Container Equipment Certification Corporation. See, e.g., 43 Fed. Reg. 26810 (June 22, 1978). The briefest glance at the trade literature is conclusive as to its marine nature. See, e.g., *Cargo Systems*, *Containerisation International*, *Container News*, *Jane's Freight Containers 1978* (10th Ed.).

[5] As a result containers generally never become "imports" and continue for the duration of their "lives" to make voyage after voyage and trip after trip without ever becoming subject to customs duty in any country.

[6] U. S. Customs Regulations, 19 C.F.R. §10.46a(f); see Customs Convention on Containers, May 18, 1956, [1969] 20 U.S.T. 301, T.I.A.S. No. 6634.

[7] A tiny percentage has been "domesticated" for use in interstate commerce (either by being manufactured in the United States or by payment of duty). Such use includes sea routes between the 48 contiguous states and Alaska, Hawaii and Puerto Rico.

Containers have been able to succeed as an international device for cargo transport because they are of standard sizes and specifications suitable for use in the transportation and handling equipment of many different nations. Perhaps 80% to 90% of the world's containers are built to the standard size and strength specifications of the International Organization for Standards in Geneva ("ISO"). ISO standard containers are generally 20 or 40 feet long, 8 feet wide and 8 or 8½ feet high.[8]

The United States interests in this industry are enormous. The United States container leasing industry alone owns approximately 600,000 TEU. When the 400,000 TEU owned by United States ship lines are added to the United States leasing ownership, total United States ownership reaches approximately 50% of the estimated world population of 2.1 million.[9] The replacement value of the 1,000,000 United States TEU is substantially in excess of $2,000,000,000.[10] and the five United States leasing com-

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[8] International Standard ISO 1496/I, *Series I freight containers —Specification and Testing, Part I General Cargo Containers* (3d. Ed.—1978-04-01).

[9] The Maritime Administration of the U.S. Department of Commerce publishes statistics on American ownership annually. While these statistics do not show foreign ownership, the Maritime Administration's *Inventory of American Intermodal Equipment 1978*, shows that at the close of 1977, United States owners, both leasing companies and ship lines, held approximately 800,000 containers (TEU). These 1977 statistics excluded one major United States leasing company which held in excess of 50,000 TEU. Most owners had added substantial numbers of containers by the end of the first six months of 1978. United States leasing companies alone added approximately 100,000 containers.

[10] A trade publication cites prices for 20 foot standard steel containers as between $2,200 and $2,500 in Europe and $1,900 in the Far East (except for Japan where presumably the price is higher). 5 *Cargo Systems* 34, 35 (No. 5, May 1978). Containers built of other materials and specialized containers are more expensive than the standard steel container. Thus, the replacement value of the United States fleet of 1,000,000 TEU could be expected to be substantially above $2,000,000,000.

panies who are members of the IICL had annual gross revenues of approximately $250,000,000 in 1977. Since all or most of these revenues are collected in dollars, the leasing industry makes a substantial contribution to the United States balance of payments.

II.

The California Tax Threatens Serious Interference With United States Foreign Commerce and With Imports and Exports.

A. *The "Home Port" Doctrine.*

The history of the United States has been strongly affected by its role as a maritime trading nation. Early in the nation's existence, the Supreme Court developed principles of respect for each state's taxation and regulation of shipping in order to reflect the nature of ships as constantly moving instruments of commerce. Those principles were called the "home port" doctrine. *Hays* v. *The Pacific Mail Steam-ship Company*, 58 U.S. (17 How.) 596 (1855); *Morgan* v. *Parham*, 83 U.S. (16 Wall.) 471 (1872).

In rejecting application of a California property tax to a ship sailing out of the Port of New York, the *Hays* case held that under the "home port" doctrine, only the state of the domicile of the vessel, or the "home port," had jurisdiction to levy property taxes. A vessel acquired no permanent situs as property in any other state. The Court's language was even broader in asserting that the tax trespassed on the domain of the federal government (58 U.S. at 599):

> And so far as respects the ports and harbors within the United States, they are entered and cargoes discharged or laden on board, independently of any control over them, except as it respects such municipal and sanitary regulations of the local authorities as are not inconsistent with the constitution and laws of the general government, to which belongs the regulation of commerce with foreign nations and between the States.

The "home port" doctrine is not only embodied in case law, but it has become codified in international tax treaties.[11] Moreover, the process of codification has extended the "home port" doctrine to containers. Bilateral tax treaties now being negotiated between the United States and other countries provide that the profits of an enterprise from the use, maintenance or rental of containers used in international traffic shall be taxable only in one of the two countries (e.g., Draft Convention for the Avoidance of Double Taxation, art. 8(3), United States-United Kingdom, *Treas. News*, Jan. 6, 1976 with text of Treaty signed December 31, 1975, now pending ratification). A concept of complete exclusion of ships from taxation has gained acceptance over the years, and numerous states have adopted provisions of constitutional or statute law prohibiting taxation of ships.[12]

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[11] For example, bilateral tax treaties commonly provide that an operator of ships and airplanes registered in the operator's country of residence, shall be exempt from tax in the other country. E.g., Convention for the Avoidance of Double Taxation With Respect to Taxes on Income, July 22, 1954, United States-Federal Republic of Germany, [1954] 5 U.S.T. 2768, T.I.A.S. No. 3133; Convention on Matters of Taxation With Related Letters, June 20, 1973, United States-Union of Soviet Socialist Republics, 27 U.S.T. 1, T.I.A.S. No. 8225.

[12] E.g., Calif. Const. art. 13, §3(l); N.Y. Tax Law §1115(a)(8) (McKinney 1965).

Containers have even less permanent situs in, and even fewer ties to, particular jurisdictions than do ships. They travel from country to country as Instruments of International Traffic and are as much subject to control by international convention as to control by the laws of any one country.[13] Leasing company containers are freely interchanged among the ships of virtually all the maritime nations of the world, and they spend most of their "lives" outside of the physical control of their owner.[14] Containers are of such transient nature that any system of allocating taxes other than by nationality of the owner has little rational basis. The "home port" doctrine would seem particularly applicable.

In recent years this Court does not seem to have dealt with taxation of vessels or maritime equipment such as containers. Some guidance, however, is provided by several cases considering state taxation of related matters under the foreign commerce and import and export provisions of the Constitution. In reviewing these cases, it should be kept in mind that the matters as to which taxation was approved were not instruments of foreign commerce, as are containers, but had, or had achieved, distinct ties to the taxing jurisdiction.

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[13] See text above and notes 4-6.

[14] The International Convention for Safe Containers reflects the commercial reality of this lessor-lessee relationship by defining the lessee as the "owner" if the lease provides that the lessee is to exercise the owner's responsibility for maintenance and examination. International Convention for Safe Containers, Dec. 2, 1972, art. II(10), *Customs Convention on Containers, 1972 and International Convention for Safe Containers,* Senate Executive X, Senate Comm. on Foreign Relations, 93d Cong., 1st Sess. (Comm. Print Nov. 15, 1973) (enters into force for United States Jan. 3, 1979).

B. *The Foreign Commerce Clause.*

This Court has considered the foreign commerce clause[15] recently in *Department of Revenue* v. *Ass'n of Washington Stevedoring Companies,* 98 S. Ct. 1388 (1978); see also *Michelin Tire Corp.* v. *Wages,* 423 U.S. 276, 290 n.11, 96 S. Ct. 535, 543 (1976). In the *Washington* case, the Court upheld application to stevedoring of a business and occupation tax of the State of Washington which excluded income attributable to interstate and foreign commerce. The Court upheld the tax on the grounds that it was only on the value of services performed within the state, was properly apportioned, did not discriminate against interstate commerce, avoided the threat of multiple burdens, and did not unfairly burden by exacting more than a just share from the interstate activity. 98 S. Ct. at 1397, 1398, 1399. As the Court later pointed out, "No foreign business or vessel is taxed." 98 S. Ct. at 1401.

Here, there is an obvious effort to tax an instrument of maritime transport and a part of the vessel itself. There is no shorebound business, part of which can be allocated to domestic and part to foreign commerce. Moreover, California made no effort to apportion. It deemed the number of containers in California on tax lien day to be representative of those there every day, but this is no different from taxing a ship in port on lien day as representative of the owner's fleet. Regardless of what the parties have stipulated, the number of containers in a state on tax lien day is arbitrary. The number of containers in any jurisdiction at one time will differ according to the season and the level of economic activity (see pp. 12-13 below). The danger of multiple burdens is also

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[15] U.S. Const. art. I, §8, cl. 3.

evident in that lien dates differ in different states; and a given container, which, like a ship, is intended always to be under way, might in a single year turn out to be in several states on the tax lien day of each such state. Nor did California make any effort to eliminate interstate or foreign elements attributable to the commerce which it taxed. As containers are integral parts of the vessels in which they travel (see p. 4 above), restoration of full freedom to the commerce here involved requires rejection of the application of the California tax to all containers.

C. *The Import-Export Clause; the Export Clause.*

In *Department of Revenue* v. *Ass'n of Washington Stevedoring Companies,* 98 S. Ct. 1388 (1978), the Court also reaffirmed the new approach to the Import-Export Clause[16] and to the Export Clause[17] established two years earlier in *Michelin Tire Corp.* v. *Wages,* 423 U.S. 276, 96 S. Ct. 535 (1976). In dealing with the Import-Export Clause, *Michelin* had abandoned the "original package" doctrine and instead analyzed whether the state tax offended any of three policies (98 S. Ct. at 1400-1401 quoting from 423 U.S. at 285-286, 96 S. Ct. at 540):

> The Framers of the Constitution thus sought to alleviate three main concerns . . . : the Federal Government must speak with one voice when regulating commercial relations with foreign governments, and tariffs, which might affect foreign relations, could not be implemented by the States consistently with that exclusive power; import revenues were to be the major source of revenue of the Federal Government and

[16] U.S. Const. art. I, §10, cl. 2.

[17] U.S. Const. art. I, §9, cl. 5.

> should not be diverted to the States; and harmony among the States might be disturbed unless seaboard States, with their crucial ports of entry, were prohibited from levying taxes on citizens of other States by taxing goods merely flowing through their ports to other States not situated as favorably geographically.

The California tax certainly offends one and probably two of these policy considerations. Few countries invoke property taxes on containers at all, and virtually none taxes the containers of foreign owners. As a result, the imposition of the California tax on the Japanese owned containers has brought protests from numerous nations and the prospect of automatic retaliation under the law of at least one (see p. 12 below). The California tax will, therefore, cause most serious interference with commercial relations with foreign governments. It clearly invades the "exclusive power" of the federal government "to speak with one voice when regulating commercial relations with foreign governments."

There is also a threat to harmony among the states, not so much arising out of imposition of a tax by a seaboard state as from the impact of retaliation upon citizens of other states. The citizens of these other states will suffer retaliation from foreign governments arising out of the California tax without having had a voice in determining the wisdom or desirability of that tax.

Department of Revenue v. *Ass'n of Washington Stevedoring Companies,* 98 S. Ct. 1388 (1978), also interprets the separate prohibition against federal taxation of exports. The Export Clause is based on the very two policies identified in *Michelin* which the California tax offends: preventing disruption of United States foreign policy and

avoiding friction among the states. Since the tax offends these two primary policies, which underly both clauses, it should be struck down, not only in regard to foreign owned containers, but also in regard to domestic owned containers. As a tax on a maritime instrument of foreign commerce, it goes beyond any state tax hitherto approved by this Court.

The threat to commercial relations with foreign governments warrants closer analysis. If California applies its property tax to foreign owned containers, retaliation by numerous foreign countries can be expected. These foreign countries include major trading partners of the United States, such as West Germany, the law of which mandates a retaliatory tax, and the United Kingdom, France, Japan, the Netherlands, Norway, Denmark, Finland and Mexico, which have protested application of the California tax in letters to the State Department. See Brief for Appellants.

California's tax will have a special competitive impact on United States leasing companies. It will be an impact of the type which economists describe as pro-cyclical because it increases during a recession and tends to aggravate recessionary effects upon the industry. Taxes imposed on containers while they are on lease to ship lines are generally passed on by the leasing company and borne by the lessee ship lines (see p. 13 below); but taxes imposed on off-lease containers must be borne by the leasing company. Currently, the United States leasing industry enjoys a high utilization factor. About 88% of its fleet was on lease during the first half of 1978. Only approximately 12% of its fleet was off-lease during that period. Thus, at that time the United States leasing industry

could have been compelled to pay property taxes, retaliatory or otherwise, on about 12% of its fleet.

The present state of world trade is, however, relatively healthy. When a recession next strikes the international economy, the utilization percentage will decline, and the current off-lease percentage of 12% could easily double. If the off-lease percentage were to double, the number of containers subject to retaliatory taxes borne by leasing companies would double, and the property taxes required to be paid by the United States leasing companies would double. Such a doubling of a non-recoverable expense would take place at the very time when the general effect of the recession would cause leasing revenues to drop and company profits to be low or non-existent. The pro-cyclical increase in retaliatory property taxation upon the leasing industry would thus be in the magnitude of 100%. A competitive penalty of this size could be expected to reflect itself further in a decline in revenues. A decline in revenues would have an effect on United States dollar payments and would have the usual multiplier effect on the industries with which the container leasing industry deals, suppliers, repairers, refurbishers, etc.

As stated above, ship line lessees normally pay any taxes on leased containers in their possession. These taxes would include property taxes, and such levies would result in severe competitive injury to United States flag steamship lines. These lines already suffer sufficient competitive disadvantages. United States leasing companies have achieved their position in world commerce, however, by leasing to foreign ship lines as well as to United States ship lines. It is anticipated that when retaliatory taxes are imposed on containers on lease to foreign ship lines, these taxes will be refunded (or application withheld)

because the containers are in the service of the foreign ship lines, but there is no guarantee that the taxes will be administered in this manner. If the United States leasing companies cannot obtain refunds or otherwise avoid these taxes on leases to foreign ship lines, the competitive penalty will be a most heavy one, regardless of the state of world trade. United States companies will be compelled to pass on the taxes in their charges to foreign ship lines as well. If these charges cause the rates of United States companies to be higher than those of their foreign counterparts, foreign ship lines will have a simple choice; they will simply lease from foreign leasing companies.

One of the reasons for the establishment of the federal government and the delegation to it of the powers hitherto possessed by the states over foreign policy and foreign commerce was that, under the Articles of Confederation, states had adopted their own taxes on imports and passed individual and conflicting regulations regarding foreign commerce. *Michelin Tire Corp.* v. *Wages,* 423 U.S. at 283, 96 S. Ct. at 539-540 (1976). Permitting California to impose a tax on containers which will cause retaliation by foreign countries will bring this country back to the conditions which prevailed before 1789. It was to establish a single foreign policy, economic as well as political, that the states delegated to the federal government their powers over these matters in 1789. The United States must "speak with one voice" to the world abroad. Its citizens cannot afford to have their policy dictated by a single, or even several, states of the Union. Taxation of the instruments of foreign commerce is a field in which federal power must claim exclusive control.

Conclusion

WHEREFORE, IICL, as *amicus curiae,* respectfully requests this Court to hold invalid the application of the California personal property tax (i) to all marine cargo containers as instruments of foreign commerce having no single situs or, in the alternative, (ii) to foreign owned containers.

Respectfully submitted,

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APPENDIX

EXHIBIT A

List of Members of IICL

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